IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 1057

INLAND STEEL COMPANY, A CORPORATION,
Petitioner,

vs.

FOREMAN M. LEBOLD AND SAMUEL N. LEBOLD,
Respondents.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

SILAS H. STRAWN,
FRANK H. TOWNER,
ARTHUR D. WELTON, JR.,
Counsel for Respondents.

THE BUNTHORP-WARREN PRINTING COMPANY, 810 WEST JACKSON, CHICAGO

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RESPONDENTS' BRIEF IN OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

May It Please the Court:

In 1936 petitioner, completely disregarding the standards and the *caveat* announced by the court below in respondents' first suit,[1] forced the dissolution of Inland Steamship Company, bought its boats, and continued its business as before. Thus frozen out, respondents instituted a second suit,[2] resulting in the decision below.

A reading of these two decisions of the court below will readily demonstrate that there is no conflict between them, and will completely dispose of the petition. For the convenience of the court the second opinion is printed as an appendix to this brief, the first appearing as an appendix

1. *Lebold* v. *Inland Steamship Co.*, 82 Fed. (2d) 451.
2. *Lebold* v. *Inland Steel Company*, 125 Fed. (2d) 369.

to the petition. The conclusions of the second decision were clearly forecast in the first, and are required, not only by the law announced in the first decision but by the overwhelming weight of authority.[3] The grounds urged by the petition are not only apocryphal, but relate largely to a hypothetical record, not to the actual record before the court.

For example, the first suggested hypothesis is that although the court below in the first case *held* that the majority might proceed with the contemplated dissolution and purchase of assets, it has now held petitioner liable to respondents for doing just that. It sounds horrific, but the court below did *not hold* that the majority might proceed. It plainly confessed to doubt as to the outcome of the announced plan, said the petitioner was a trustee, and stated: "We do not mean to imply that the circumstances that may hereafter develop, taken in connection with what has developed, may not bring appellants [respondents here] within that line of authorities which recognizes a right of action for an unfair advantage taken by a majority" (82 Fed. (2d) 451, 455).

A second suggested hypothesis is that at the dissolution sale petitioner paid fair value for the assets of the Steamship Company—the implication being that such payment was for *all* the assets. All that petitioner even pretended to pay for was the tangible physical assets. For these it paid fair value—$1,120,000, the equivalent of $700 per

3. *Pepper* v. *Litton*, 308 U. S. 295, 306; *Southern Pacific Company* v. *Bogert*, 250 U. S. 483, 487, 491; *Jones* v. *Missouri-Edison Electric Co.*, 144 Fed. 765, 771 (C. C. A. 8th); *Wheeler* v. *Abilene Nat. Bank Bldg. Co.*, 159 Fed. 391, 393, 394 (C. C. A. 8th); *Ervin* v. *Oregon Ry. & Nav. Co.*, 27 Fed. 625, 630-632; *Marks* v. *Merrill Paper Co.*, 188 Fed. 850, 854, 855; *In re Doe Run Lead Co.*, 223 S. W. (Mo.) 600, 609, 610; *Morse* v. *Metropolitan etc. Co.*, 100 Atl. (N. J. Eq.), 219, 221 (affirmed at 102 Atl. 524); *Baillie* v. *Columbia Coal Mining Co.*, 136 Pac. (Ore.) 954, 974; *Moore* v. *Lewisburg, etc. Co.*, 93 S. E. (W. Va.) 762, 765; *Major* v. *American Malt Co.*, 181 N. Y. S. 152, 153; *Kavanaugh* v. *Kavanaugh Co.*, 123 N. E. (N. Y.) 148, 151; *Hyams* v. *Calumet & Hecla Mining Co.*, 221 Fed. 529, 543 (C. C. A. 6th); *Farmers Loan & Trust Company* v. *N. Y. & Northern R. R. Co.*, 150 N. Y. 410, 44 N. E. 1043. See also Berle & Means, "The Modern Corporation and Private Property" (page 251).

share. But the court below in the first case had already held that respondent's stock was worth more than $700 per share, which was only another way of saying that *all* the assets were worth more than that figure. Therefore, petitioner's assertion that it paid "full fair value" for the assets of the subsidiary is in the teeth of the holding of the court below in the first case.

A third major hypothetical assumption is that the question of the measure of damages was not an issue before the court below. The District Court made four findings thereon [prepared by petitioner's counsel], numbers 20, 21, 22 and 26 (R. 226, 227), which are assigned as error directly (R. 233, 234) and indirectly (*i. e.*, numbers 42-48, R. 237, 238). Our assignment #51 reads:

> "The court erred in failing to hold that the plaintiffs as minority stockholders are entitled to be paid by the Steel Company the fair value of their stock in the Steamship Company viewed as a going concern, having a demonstrated earning capacity." (R. 238.)

The issue was clearly raised on the appeal. Indeed, the petitioner has swung between two positions—one, that respondents were not damaged (which would have required a negative decision on the proposition just quoted); and the other, that even if there was damage, there was no breach of petitioner's fiduciary obligation, and therefore no remedy. Both points were extensively argued. The case presents a situation where the answer to the question of remedy is found in the answer to the question of damage. The court was undoubtedly right in its conclusion, and in announcing its conclusion, on the question of damage. It is the settled policy of the law that there should be an end of litigation.

With these general considerations in mind, we turn to the statement and the particular points of the petition.

STATEMENT.

Petitioner's statement is so argumentative and controversial, that the following very short statement is submitted.

In 1935 petitioner, majority stockholder in complete control of its 80% owned subsidiary, Inland Steamship Company, sought to buy from respondents, at $700 per share, their 18% of the subsidiary's stock. In the face of an excellent 24 year earnings and dividend record (the latter averaging $100 per share annually)[4] respondents refused the offer, said they were willing to sell at a fair value, and suggested arbitration. Petitioner said it would not arbitrate with outsiders the price it would pay for something it wished to buy (R. 82, 83).

The subsidiary's business was transportation by water—almost entirely of ore for petitioner. The petitioner threatened respondents that unless they sold their stock to the petitioner at the price of $700 per share set by itself, petitioner would sever traffic relations with the Steamship Company: the latter would then have no business, would be dissolved, and, at the dissolution sale petitioner would buy in the boats and carry on the business.

The record establishes beyond controversy that the dissolution was adopted for the sole *purpose* of eliminating respondents as minority stockholders (R. 82). The sole reason for adopting it was respondent's refusal to sell the stock to the majority at the price fixed by the majority—a price expressly held by the court below in the first case to be less than fair (82 Fed. (2d) 351, 356). The sole

4. For the eleven year period 1925-1935 average annual earnings were just under $200 per share, average annual dividends $116 per share (R. 197).

objective and the sole accomplishment were to eliminate respondents from participation in the common enterprise. Petitioner sought to, and but for the decision of the court below, would have, derived an advantage from disposition of the subsidiary's assets not only at the expense of the respondents but exactly in proportion to that expense.

Prior to the dissolution a vice president both of petitioner and of the Steamship Company said, with respect to the dividends paid the latter's stockholders: "I have got my eye on the part that we do not get" (R. 100); that "it gripes me very much * * * to pour a golden stream to the minority stockholders" (R. 99). After the dissolution he said that "the principal economy in direct operation comes from operating at cost without a profit * * * to the extent that we did not own the stock, the profit did not flow to us. It was *this* profit that did not flow to us that was *the major item of added cost*" (R. 58; italics supplied).

This brief statement, in conjunction with the quite full statements of the facts found in both of the opinions, adequately presents the case. There should, however, be some reference to some of the misstatements in the petition.

At page 3 (in bold face) there is the statement that "petitioner was under no obligation, prior to dissolution of the Steamship Company, to tender its cargoes to the Steamship Company for carriage"—because there was no contractual arrangement of any kind between the two companies as to the carriage of Steel Company's freight. But the court in its first opinion said, as to this question, "There was no express contract between the two companies, but the tonnage was carried by *original arrangement*, succeeded by *tacit understanding*, at the going or market rates, which are not governed by statute but are the result of competition" (82 Fed. (2d) 351, 352).

The soundness of this observation is borne out by the testimony of Mr. Randall who, in speaking of another Steel Company which owned 49% (or 51%) of a transportation company, said: "I know their traffic is *bound* to that fleet because of their ownership" (R. 51). The court below recognized this factor in commenting on petitioner's threat to take its business away from the Steamship Company: "It should be remembered that, if it [petitioner] does so, it will thereby wipe out profits, 80% of which belongs to it, or if it becomes the owner of all the assets of the latter, 100%" (82 Fed. (2d) 351, 355).

At page 5 of the petition it is stated that: "In 1934 Steel Company determined to carry its freight at cost either in its own ships or in those of a wholly-owned subsidiary". According to the testimony of petitioner's witness, the *first* decision was that the Steel Company's traffic could be transported more economically than through the then existing arrangement with the Steamship Company, either by chartering one or more steamers, by seeking lower rates from other carriers, or by buying other boats and setting up an Inland Steel fleet (R. 96). The real decision was to eliminate the minority.

It is said on page 7 of the petition that the sale and distribution "is not claimed to have been in any way unfairly held or made." So far as mechanics are concerned, this may be accepted as accurate, but, of course, it is the respondent's position that the sale and distribution, just like everything else that was done, was part of a fraudulent scheme, and, therefore, tainted with the same fraud.

So far as the case is concerned, it obviously presents a "violation of rules of fair play and good conscience" (*Pepper* v. *Litton*, 308 U. S. 295, 310).

ARGUMENT.

I.

The Decision of the Court Below in the First Case Cannot Possibly Be Deemed a Holding that the Majority's Proposed Action Was Not Fraudulent.

It may be doubted that anything need be added to the opinion in the first case to demonstrate the unsoundness of the proposition advanced by petitioner under Point I of its argument.

The premise of petitioner's argument here (pet. p. 13) is that the court below "*necessarily* decided that the contemplated dissolution and sale were not fraudulent or improper." It should be noted that petitioner is utterly unable to point to the passage of the opinion where the court so held. The simple fact is the court plainly said that until the contemplated action was taken, there were no facts before the court to serve as a basis for a finding of fraud. By the same token, there was no basis for a finding that there was no fraud.

The court made it very clear that it was considering *only* the question whether it should enjoin the holding of a projected corporate meeting. In answering that question the court said:

> 'There has *as yet* been no disposition of the assets or loss to the minority. We cannot say that there will be any such loss. *Thus far* the majority, though it has admitted its motives, *has done only* that which the statute permits it to do, call a meeting for dissolution. *This* it has a legal right to do. It *may* proceed to a dissolution, but what will happen *then* or *thereafter* is *not now* before the court, and cannot *now* be made the basis for a finding of fraud" (82 Fed. (2d) 351, 354, italics supplied).

In other words, the court said plainly that whatever the *plan* of the majority stockholders might be, the facts that would result from its consummation were not then before the court and could not be made a basis for a finding of fraud. But the motive was clearly characterized when the court said:

> "We would be more favorably impressed by the protestations of good faith of appellee's officers had they in their capacity of representatives of the dominant company shown a willingness to submit to arbitration the value of appellants' minority stock. The majority stockholder may believe that it is entirely fair, but its position renders impartiality difficult, for it is compelled to say, 'Let not thy right hand know what thy left hand doth.' In view of the frankly admitted desire of the majority to acquire the stock of the minority, its frank confession that the payments of profits to the minority brings only chagrin and dissatisfaction to the majority, the threat that, unless the minority will sell to it at its own price, it will force dissolution and liquidation of assets and thus produce an opportunity to purchase at a satisfactorily low market price all the physical assets, we confess to some doubt as to eventual results. That degree of fairness required of parties in a dominant situation, or of fiduciary representatives of corporations, or of majority stockholders to the minority, making legal duress impossible, must be present before a court of equity may rest quiescent." (82 Fed. (2d) 351, 355.)

Beyond that, the court in its first opinion clearly forecast the conclusion in the second. It was announced that the majority (the petitioner) stood in the position of a fiduciary to the minority (respondents) and was subject to "the burden of the utmost of scrupulous fair dealing" with that minority; that the majority may not force a sale to itself at less than full value; that the minority must receive its pro rata share of the revenue or property *and* the fruits of the capital investment"; that the price of $700 per share offered by the majority to the stockholders was inadequate

because it was based on asset value alone, and did not consider the earnings record; and that the result of the contemplated plan of dissolution and sale would mean that the petitioner would become the owner of all the profits flowing from the Steamship Company's transportation business.

Put otherwise, the court clearly indicated that the proposed plan would result in an appropriation by the petitioner as majority stockholder of all of the assets of and profits from the Steamship Company's business without paying therefor, a clear breach of petitioner's fiduciary obligation.

Petitioner's misunderstanding of the opinion below is nowhere more clearly demonstrated than in the following sentence (pet. p. 6): "It is highly significant to note that in the extensive *obiter dicta* indulged in by the Circuit Court of Appeals in its opinion, deciding to affirm the lower court, it did not indicate that if the dissolution and sale were carried out as proposed, it would hold the same to be a fraud."

Of course, it was no part of the court's function to act as counsel to the petitioner, and there was no burden upon it to advise petitioner what the court would decide if the proposed fraudulent plan was carried out. And yet, the simple application of the principles announced in the first case made the answer clear.

Typical of petitioner's argument is the following sentence on page 14: "It is merely because the court attempted to qualify its affirmance, as noted above, that respondents contend that the two decisions are not in conflict."

A fair reading of the opinion makes it clear that the court did not merely attempt to qualify its affirmance. It very adequately and clearly qualified it. Furthermore, it is not only the respondents who contend that the two decisions are not in conflict. It so happened that both appeals

were heard by the same three judges of the Circuit Court of Appeals, and each opinion was written by the same judge. Before the decision of the second case petitioner argued extensively that the first decision was *res adjudicata*. It again argued this point on the petition for rehearing. In the face of this construction of their own decision by the same court, it seems quite unnecessary that respondents should have to contend that there is no conflict.

We do, of course, believe that to be the true interpretation of the opinions and, as we have suggested before, the opinions themselves abundantly demonstrate this to be so. It may be, as petitioner says on page 15, that the court might have enjoined the projected offer. As events have turned out, it would, perhaps, have been a good thing if it had done so. But it hardly lies in the petitioner's mouth to complain of this nice balancing of a purely discretionary matter, when the result in the first case was exactly what petitioner then urged upon the court.

Nor is it fair for petitioner to refer to the first opinion as though it were merely affirmed "without prejudice." Every question, except the right of the majority to call a meeting, was carefully preserved for future consideration. The court said:

> *"But this affirmance and the dismissal by the court below will be without prejudice to the right of appellants hereafter to present the facts herein presented in connection with such further facts, if any, as bring about a situation within the doctrine recognizing causes of action in minority stockholders"*. (82 Fed. (2d) 351, 356).

It was clearly within the power of the court below to reserve the questions that it thus reserved. Its ultimate conclusion upon those questions is the only decision possible in view of the principles announced in the first case.

II.

There Is No Conflict With the First Circuit Case of May v. *Midwest Refining Co.*

It must be first noted here that it is scarcely accurate for petitioner to say that the Circuit Court of Appeals has held that petitioner defrauded respondents merely because it purchased the ships at the dissolution sale. As the court said: "The business was not discontinued; defendant took over the boats, it continued to operate them, it continued to devote them to the same transportation that they had always carried on—the only difference being that now the latter realizes all the profit which results from such transportation and the minority stockholders get none of it" 125 Fed. (2d) 369, 373.

In view of the court's finding that the respondents' stock was worth more than $700 per share, and the admitted fact that respondents did not receive even that much out of the proceeds of the sale, it is patent that the consideration paid by petitioner was inadequate. This was an essential ground of the decision below. In *May* v. *Midwest Refining Co.*, 121 Fed. (2d) 431, at page 438, the court itself noted that "we have before us no allegation of inadequacy of consideration." It is impossible to find any conflict between two decisions when the ground upon which one is predicated was not even an issue in the other.

III.

There Is No Conflict With the West Virginia Decisions.

It should be noted that under this third subdivision petitioner would forget that it is trying to justify its conduct as a trustee. It seems to think that such justification can be found in the alleged absolute right of a stockholder in a

West Virginia corporation to vote in his own interest, even against the interest of the minority. The ready admission that petitioner's action may be justified upon this basis provides by itself an adequate answer to the petition.

The West Virginia statute upon which petitioner relies authorizes a 60% majority stockholder to *discontinue the business* of a corporation. Petitioner did not discontinue but appropriated the business of the Steamship Company, and the court so found. There is no law in West Virginia or elsewhere that gives sanction to such an appropriation at the expense of the minority stockholders.

The very case cited by petitioner (*Thurmond* v. *Paragon Colliery Co.*, 82 W. Va. 49, 95 S. E. 816) is relied upon by the court below, and establishes that a majority stockholders' vote "must not be so antagonistic to the corporation as a whole as to indicate that their interests are wholly outside of the interest of the corporation *and destructive of the interests of the minority stockholders.*" (See 125 Fed. (2d) at page 374.)

The other West Virginia case referred to, *Tierney* v. *United Pocahontas Coal Co.*, 85 W. Va. 545, 102 S. E. 249, points out in the very passage quoted that the transaction must be entirely fair and must prejudice the rights of *no* interested party. The court said, further: "In a case like this, where the purchaser of the property is also in effect the seller, the utmost good faith is required" (102 S. E. at p. 255) and held that the minority was not bound by the sale which was held to be at an inadequate price.

The nub of the matter is demonstrated in petitioner's discussion of this court's opinion in *Pepper* v. *Litton*, 208 U. S. 295. It is asserted that the court below relies upon this decision as authority for the proposition that it is *ipso facto* a breach of trust for a parent corporation to vote for the dissolution of its subsidiary, against the interests of the minority stockholders thereof, and to purchase the sub-

sidiary's physical assets for a full fair price and use them in its business.

Pepper v. *Litton* stands for the ordinary principles of fair play. It was not relied on by the court below as authority for the proposition as stated by petitioner, nor does that proposition correctly represent the decision in this case.

The court below decided that petitioner set out to acquire the assets and business of the Steamship Company, and that it did acquire such assets and business without paying therefor. Liability attaches to petitioner in such a case as surely under the principles of *Pepper* v. *Litton* as under the many decisions representing the weight of authority and relied on by the court below in its two opinions.

IV.

The Court Below Properly Laid Down the Rule to Be Used in Determining Respondents' Damages.

It seems unnecessary to add to what has already been said with respect to petitioner's complaint under its fourth point. Certainly, it is sufficient to say that the question of injury to the plaintiffs was inherent in the case. Petitioner recognized this, for it introduced evidence upon the question of the value of respondents' stock (R. 60, 67). It submitted findings thereon to the District Court (R. 226, 227); it was the subject of assignment of error (R. 233, 234), and it was argued in the briefs.

By announcing the rule to be applied in ascertaining the amount of respondents' damages, the court below avoided the possibility of yet another appeal after the taking of evidence upon this question. It is impossible to see any sound basis for criticism of the court's obviously correct conclusion upon this point.

Conclusion.

In conclusion it is respectfully submitted that the petition presents neither grounds nor reason for granting the writ prayed for.

Respectfully submitted,

Silas H. Strawn,
Frank H. Towner,
Arthur D. Welton, Jr.,
Counsel for Respondents.